

IDAHO OUTLOOK

NEWS OF IDAHO'S ECONOMY AND BUDGET

STATE OF IDAHO

DIVISION OF FINANCIAL MANAGEMENT

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“What did you do on your summer vacation?” School children dread this phrase because it marks the beginning of another school year. Some kids will use this opportunity to relive their summer travels. Those who traveled across our great country were treated to magnificent vistas deserving of an Aaron Copland soundtrack. For some vacationers, this opus was augmented with refrains of “Are we there yet?” from the backseat chorus. But kids weren’t the only ones asking this question this summer. Economy watchers anxious to know whether our nation is on the road to sustained business recovery have also been singing this tune.

The answer to this question depends on whom you ask. According to the National Bureau of Economic Research, the recovery began in December 2001. However, for most Americans, this news is about as appealing as driving two weeks to visit the world’s second largest ball of yarn. This is not to say Americans haven’t been good travelers. All along this journey they have kept their spirits up, despite experiencing some trying times. And they spread their good cheer by spending freely, not just on trinkets found at souvenir shops, but on major purchases. In fact, they may be riding in a new car financed by a low- or no-interest deal.

This economic recovery road trip officially began about a year and a half ago. But for some it has been as pleasant as riding through Death Valley without air conditioning. The employment situation has been disappointing. The manufacturing sector has been particularly hard hit, shedding nearly 16% of its jobs since July 2000. The economy has failed to generate significant job growth to date

during the recovery. Because of the weak job picture, the unemployment rate continued to rise long after the recovery started. It is hoped the unemployment rate has reached its zenith, but more data is needed before this can be confirmed. The labor market is expected to improve beginning early next year. However, the unemployment rate will seem to improve slower than the line to Disneyland’s Indiana Jones and the Temple of Doom attraction. It is forecast to average about 6.0% over the next few years.

As with most road trips, the recovery has had its share of close calls. Most recently, some have feared increasing consumer debt would threaten the recovery. The U.S. household debt-service is at a record level. But the rise in household debt cannot be blamed on a sudden spending spree. Instead, records show the ratio of consumer debt to disposable income has been rising for nearly three decades. One reason for this is credit has become available to a growing portion of the population over time. Lower interest helped maintain this trend during the current recovery. Interestingly, the U.S. household debt-to-income ratio compares favorably to many other developed countries. For example, households in Japan, Germany, and the United Kingdom have higher ratios of debt to income. In fact, Standard and Poor’s David Wyss points out that of industrialized countries only Italy had a lower debt-to-income ratio than the U.S. The rise in private debt does not seem to be a threat to the recovery.

Likewise, public finances should not be a problem in the short term. The ratio of the federal budget deficit to GDP should remain below the 5% threshold that was breached in the early 1980s and 1990s. The ratio of U.S. federal debt to GDP should be around

40% over the next couple of years, which is well below its recent high of 50% in the early 1990s. While the country’s books are relatively sound, the U.S. debt could create problems further down the road. Persistent, high deficits could increase federal government borrowing needs. This would put upward pressure on long-term interest rates that would lower the trajectory of U.S. economic growth. But that is a problem for another day.

We are not there yet, but we are close. Traditionally, Federal Reserve policy was a good indicator of where the economy was headed. For example, a tightening of the central bank’s policy was a sign the economy was past the early recovery stage and on solid ground. The presidential race complicates matters this year because the Federal Reserve is hesitant to change its policy during an election year. The Federal Reserve is expected to tighten after the election. Thus, it can be deduced that sustained growth will commence before then.

Given the information available it appears the economy arrives in 2004. However, as with any long trip, emergencies can slow it down. The economy has certainly had its share during this recovery, including the Iraq War and corporate accounting scandals. Despite these challenges, the economy has moved forward. Although these may have delayed the trip, they have not cancelled the vacation.

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General Fund Update

As of August 31, 2003

<u>Revenue Source</u>	\$ Millions		
	FY04 Executive Estimate ³	DFM Predicted to Date	Actual Accrued to Date
Individual Income tax	882.8	127.8	135.7
Corporate Income tax	96.7	6.7	7.3
Sales Tax	865.6	150.9	156.4
Product Taxes ¹	45.6	8.0	7.8
Miscellaneous	150.9	38.0	38.2
TOTAL GENERAL FUND²	2,041.6	331.4	345.4

1 Product Taxes include beer, wine, liquor, tobacco and cigarette taxes
2 May not total due to rounding
3 Revised Estimate as of August 2003, adjusted for 2003 legislative actions

General Fund revenue was \$10.0 million higher than expected in August. This makes two consecutive months of stronger than expected revenue collection, and brings the fiscal year-to-date excess to \$14.0 million. The vast majority of this strength is due to the individual income tax and the sales tax.

Individual income tax revenue was \$6.0 million higher than expected in August. On the collection side, filing payments were \$0.2 million higher than predicted and withholding collections were \$4.5 million higher than predicted. On the payout side, refunds were \$0.9 million lower than expected and miscellaneous diversions were \$0.3 million lower than expected.

Year-to-date individual income tax revenue is now \$7.9 million (6.2%) higher than expected.

Corporate income tax revenue was \$1.0 million higher than expected in August. Filing payments were \$1.7 million higher than predicted for the month, while quarterly estimated payments were \$1.9 million lower than predicted. Refund payments were \$1.1 million lower than expected for the month, while miscellaneous diversions were \$0.1 million lower than expected. Corporate income tax collections are now \$0.6 million (9.0%) higher than expected for the fiscal year to date.

Sales tax revenue was \$3.2 million higher than expected in August. This revenue category is now \$5.5

million (3.6%) ahead of the year-to-date expectations.

Product taxes and miscellaneous revenues were both exactly on target in August. Within the miscellaneous category weakness in the estate tax and insurance premier tax was afferent by strength in interest earnings.